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Income Tax Act, 2025 — India's New Tax Code Replaces the 64-Year-Old 1961 Act

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✍ WHY IN NEWS

The Income Tax Act, 2025 — which received Presidential assent in August 2025 — became operative from April 1, 2026 (Assessment Year 2026-27). It replaces the Income Tax Act, 1961, a legislation that had accumulated 64 years of amendments, Finance Act insertions, court interpretations, and CBDT circulars into a document of 819 sections across 47 chapters. The new Act reduces this to 536 sections in 23 chapters, introduces the unified “Tax Year” concept, and codifies digital-first tax administration.

WHY THE 1961 ACT NEEDED REPLACEMENT

The Complexity Problem

The Income Tax Act, 1961, began as a 298-section document at inception. By 2025, it had grown to 819 sections through 64 successive Finance Acts, each adding provisions, exceptions, exceptions-to-exceptions, and cross-references that made the Act increasingly difficult to interpret without professional help.

The consequences of complexity:

- **Litigation explosion:** India had approximately 5 lakh pending direct tax cases before Income Tax Appellate Tribunals (ITAT), High Courts, and the Supreme Court — many arising from ambiguous drafting rather than genuine evasion disputes
- **Compliance cost:** MSME compliance costs for income tax were estimated at 1-3% of turnover — a regressive burden hitting smaller businesses hardest
- **Interpretive divergence:** The same provision often had multiple authoritative interpretations across different High Court jurisdictions, creating geography-based tax outcomes

Previous Reform Attempts

This is not India's first attempt at a new direct tax code:

- **Vijay Kelkar Committee (2002):** Recommended simplification; not implemented
- **Direct Taxes Code (DTC) Bill, 2009:** Introduced but lapsed; reintroduced 2010; withdrawn 2014
- **Akhilesh Ranjan Committee (2019):** Recommended structural overhaul; led eventually to the 2025 Act
- **Budget 2024 announcement:** FM Nirmala Sitharaman announced a comprehensive review in her interim Budget; the 2025 Act is the outcome

WHAT CHANGED — STRUCTURE AND LANGUAGE

The Core Structural Changes

1. From 819 Sections to 536 Sections The reduction is not achieved by removing provisions — it is achieved by:

- Consolidating related provisions that were split across multiple sections
- Moving repetitive provisions into single operative sections
- Eliminating provisions that had become redundant (e.g., sections relating to abolished taxes like Fringe Benefit Tax, Banking Cash Transaction Tax)

2. From 47 Chapters to 23 Chapters Logically related topics are grouped together. For example:

- All deductions (previously spread across Chapter VI, Chapter VI-A, and multiple scattered sections) are consolidated into a single Chapter on “Deductions from Total Income”
- Procedural provisions (assessment, appeal, revision, rectification) are in a single Chapter on “Procedure”

3. The “Tax Year” Reform — Ending a 64-Year Confusion

Old system (1961 Act):

- **Previous Year:** The year in which income is earned (April 2025–March 2026)
- **Assessment Year:** The year in which the previous year’s income is assessed and taxed (April 2026–March 2027)
- Taxpayers routinely confused the two when filing returns and making advance tax payments

New system (2025 Act):

- Single “Tax Year” = the financial year in which income is earned AND assessed
- Tax Year 2025-26 = income earned and assessed in April 2025–March 2026
- Simplifies the vocabulary and eliminates the year-shift confusion in return filing

4. Language Simplification The 1961 Act used complex run-on sentences with embedded provisos. The 2025 Act uses:

- **Tables** for graduated rates (instead of dense prose)
- **Formulas** for computed values (instead of text descriptions of calculations)
- **Definitions** front-loaded in each Chapter (instead of buried in the middle of provisions)

WHAT DID NOT CHANGE

Tax Rates: The 2025 Act is a structural reform, not a rate revision. Income tax slabs, surcharge rates, cess, and TDS rates are unchanged from what was already in force under successive Finance Acts. The Budget 2026 tax changes (nil tax up to ₹12 lakh; revised slabs) were implemented via the Finance Act 2025; the Income Tax Act, 2025 carries these rates forward in the new structure.

Tax Base: All existing heads of income (Salary, House Property, Business/Profession, Capital Gains, Other Sources) are retained.

Deductions: Section 80C (investments), 80D (health insurance), 80G (donations), HRA exemption, LTA — all retained. The provision numbers change; the entitlements do not.

Assessment Procedures: Faceless assessment (introduced 2020), faceless appeals (2021), and annual information statements are carried forward and given more explicit statutory basis.

THE DIGITAL TAX ADMINISTRATION CODIFICATION

What Faceless Assessment Means

Under the old system, income tax assessment was done by the Assessing Officer (AO) in the taxpayer's local jurisdiction. This created:

- Discretion and potential for harassment
- Geographical inconsistency in outcomes
- Physical presence requirements

The 2025 Act formally codifies:

- **Faceless Assessment:** Cases are randomly allocated to AOs across India; the taxpayer never knows who is assessing them; all communication is digital
- **Faceless Appeals:** Appeals against assessment orders go to randomly allocated appellate officers; no in-person hearings
- **Centralized Processing:** Returns processed at Centralized Processing Centres (CPCs) – currently in Bengaluru and Mysuru

Annual Information Statement (AIS)

AIS – the comprehensive tax information statement showing all income, TDS deductions, financial transactions, and foreign remittances as reported by third parties – is given formal statutory status under the 2025 Act. Taxpayers can access and correct their AIS before filing returns.

WHO BENEFITS MOST

| CATEGORY | BENEFIT |
|----------------------|---|
| Individual taxpayers | Simpler language; single Tax Year concept; clearer deduction provisions |
| MSMEs | Reduced compliance cost from clearer provisions; fewer interpretation disputes |
| Tax practitioners | More logical structure; reduced cross-referencing |
| Tax administration | Formal codification of digital procedures; reduced litigation on procedural grounds |
| Foreign investors | Cleaner, more internationally legible tax code |

WHAT CRITICS SAY

“Structure is not substance”: Critics argue the 2025 Act solves the presentation problem (complex language, too many sections) without addressing the substantive problems — transfer pricing disputes, capital gains tax complexity, taxation of digital services, and the income-vs-capital distinction in complex financial instruments.

No reduction in dispute provisions: While section count is reduced, the dispute resolution provisions (appeal to CIT(A), ITAT, High Court, Supreme Court) are unchanged. The proliferation of disputes is driven by ambiguous substantive provisions and aggressive assessment — not section count.

The simplification paradox: Some experts note that “simplification” through tables and formulas can create new ambiguities — especially when a complex proviso is replaced by a formula that handles the common case but not edge cases.

HISTORICAL CONTEXT — INDIA’S DIRECT TAX ARCHITECTURE

Timeline

| YEAR | DEVELOPMENT |
|------|---|
| 1860 | Income tax first introduced in India (by British government; temporary, to finance war costs) |
| 1886 | First Income Tax Act of India |
| 1922 | New Income Tax Act (1922 Act) — governed pre-independence India |
| 1961 | Income Tax Act, 1961 — replaced the 1922 Act; operative from April 1, 1962 |
| 2025 | Income Tax Act, 2025 — replaces the 1961 Act; operative from April 1, 2026 |

Direct Tax Administration Structure

Ministry of Finance → Department of Revenue → CBDT (Central Board of Direct Taxes)

- CBDT issues circulars and notifications implementing the Act
- Income Tax Department: ~75,000 officers; 18 Principal Chief Commissioner regions
- Assessment under the 2025 Act: Primarily faceless; physical assessment only in specific exempted categories

UPSC RELEVANCE

Income Tax Act, 2025 (effective April 1, 2026, AY 2026-27); replaces 1961 Act; 536 sections, 23 chapters; Tax Year concept; CBDT; faceless assessment; Presidential assent August 2025.

MAINS GS-3:

“The Income Tax Act, 2025 is a structural simplification, not a substantive reform. Critically examine this claim and suggest areas where substantive reform is still needed in India’s direct tax system.”

MAINS GS-2:

“Direct tax administration in India — how has digital technology (faceless assessment, AIS, CPC) changed the relationship between the taxpayer and the tax administration?”

INTERVIEW:

“India replaced a 64-year-old tax act — is this a landmark reform or a repackaging? What would genuine tax reform look like?”

★ FACTS CORNER — KNOWLEDGEPEDIA

INCOME TAX ACT, 2025:

Replaces: Income Tax Act, 1961 (64 years old; operative since April 1, 1962)

Presidential assent: August 2025

Operative from: April 1, 2026 (AY 2026-27 = Tax Year 2026-27)

Sections: 536 (vs 819 in 1961 Act)

Chapters: 23 (vs 47 in 1961 Act)

Key structural reform: “Tax Year” replaces dual “Previous Year” + “Assessment Year” system

Administered by: CBDT (Central Board of Direct Taxes), Department of Revenue, Ministry of Finance

KEY TAX RATES (CARRIED FORWARD FROM FINANCE ACTS — UNCHANGED):

Nil tax: Income up to ₹12 lakh (with standard deduction, under new regime)

New tax regime (default): 5% (3-7L), 10% (7-10L), 15% (10-12L), 20% (12-15L), 30% (above 15L)

Surcharge: 10% (50L-1Cr), 15% (1Cr-2Cr), 25% (2Cr-5Cr), 37% (above 5Cr) — on tax

Health & Education Cess: 4% on (tax + surcharge)

FACELESS ASSESSMENT FRAMEWORK:

Introduced: 2020 (Transparent Taxation — Honouring the Honest platform)

Statutory basis: Now codified in Income Tax Act, 2025

Cases excluded from faceless: Search-related, international tax, specific high-value transactions

INDIA'S DIRECT TAX COLLECTIONS (FY 2024-25):

Total direct tax collection: ₹22.28 lakh crore (record high)

Personal Income Tax: ₹12.01 lakh crore

Corporate Tax: ₹9.11 lakh crore

Taxpayer base: ~97 million PAN holders; ~82 million ITR filers

PREVIOUS REFORM ATTEMPTS:

DTC Bill 2009 (Manmohan Singh govt): Introduced, lapsed

DTC Bill 2010: Reintroduced, withdrawn 2014

Akhilesh Ranjan Committee (2019): Led to the 2025 Act

OTHER RELEVANT FACTS:

ITAT (Income Tax Appellate Tribunal): Quasi-judicial body; appeals from CIT(A) decisions; ~90 benches across India

AIS (Annual Information Statement): Comprehensive pre-filled tax information for each taxpayer; accessible on IT portal

Advance Tax: Four instalments (June 15: 15%, September 15: 45%, December 15: 75%, March 15: 100%) — unchanged

Heads of Income (unchanged): Salary, House Property, Business & Profession, Capital Gains, Other Sources

Sources: [Income Tax Act, 2025 \(MoF\)](#), [CBDT](#), [PIB](#), [GKToday](#)

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